FEDERAL RESERVE BANK OF NEW YORK

NEW YORK, N.Y. 10045-0001

AREA CODE 212-720-5000

September 30, 2002

To: The Individual Responsible for Preparing the Financial Statements for Large Bank Holding Companies (FR Y-9C) Located in the Second Federal Reserve District

Subject: Bank Holding Company Reporting Requirements for September 30, 2002

Enclosed are two copies of the following report forms and instructions for the September 30, 2002 reporting date:

(1) Consolidated Financial Statements for Bank Holding Companies (FR Y-9C);

(2) Parent Company Only Financial Statements for Large Bank Holding Companies (FR Y-9LP);

(3) Quarterly Financial Statements of Nonbank Subsidiaries of Bank Holding Companies (FR Y-11Q); and

(4) Consolidated Bank Holding Company Report of Equity Investments in Nonfinancial Companies (FR Y-12).

There are no revisions to the FR Y-11Q for this quarter. Significant accounting updates have been provided in Attachment 1.

FR Y-9C and FR Y-9LP Instructions

On the FR Y-9C, instructional clarifications were made to Schedule HI, Consolidated Report of Income, to clarify the reporting of premium revenues from reinsurance underwriting operations. In addition, an instructional clarification regarding cumulative preferred stock instruments included in minority interest in consolidated subsidiaries was made to Schedule RC-R, Regulatory Capital.

On the FR Y-9LP and FR Y-12 there were a minor instructional clarifications. All FR Y-9C, FR Y-9LP, and FR

Y-12 clarifications are summarized in the Attachment 2.

Reports Submission

An original and two copies (one-sided) of each completed bank holding company report must be returned to this bank by mail or messenger by the dates listed below. Under the Regulatory Reports Monitoring Program, the timeliness of receipt of these reports will be monitored. Earlier submission would aid this Bank in reviewing and processing the reports and is encouraged.

The submission deadline for the **FR Y-9C, FR Y-9LP, and FR Y-12** is **Thursday, November 14, 2002**. Any FR Y-9C, FR Y-9LP, or FR Y-12 reports received after 5:00 p.m. on November 14th will be considered late unless postmarked by Monday, November 11th or sent by overnight service by Wednesday, November 13th.

The submission deadline for the **FR Y-11Q** is **Friday, November 29, 2002**. Any FR Y-11Q report received after 5:00 p.m. November 29th will be considered late unless postmarked by Tuesday, November 26th or sent by overnight service by Thursday, November 28th.

Submission of initial data via facsimile, even if prior to this deadline does not constitute timely filing. In view of this, please be sure that completed reports are submitted on time to:

Federal Reserve Bank of New York
Statistics Function
Administrative Support Staff
33 Liberty Street, 4th Floor
New York, N.Y. 10045

Edit Checklist

The staff of this Bank will monitor whether banking organizations are meeting their basic reporting requirements through the use of “validity edits”. Enclosed are the updates to the monitoring edits. Please note these updates to ensure your institution meets these edit tests. Also, to avoid common reporting errors, we are now providing a list of edit checks which we perform between the FR Y-9LP and FR Y-9C reports.

Electronic Submission Option

This Bank offers bank holding companies the option of submitting their FR Y-9C, FR Y-9LP, FR Y-11Q and FR Y-12 reports electronically. Any bank holding company interested in submitting these reports electronically should contact Carolyn Polite at (212) 720-5415 for information concerning the procedures for electronic transmission. Bank holding companies choosing to submit these reports electronically must maintain in their files a signed printout of the data submitted. The cover page of the Reserve Bank supplied report forms should be used to fulfill the signature and attestation requirement and this page should be attached to the printout placed in the bank holding company's files.

In addition, we now offer distribution of this letter, report forms, and instructions via e-mail. If you are interested in receiving this electronically, please fax the attached form to Erica Baker at (212) 720-7300.

Website

Report forms and instructions for the FR Y-9C, FR Y-9LP, FR Y-11Q and FR Y-12 are also available on the Federal Reserve Board’s web site at ***www.federalreserve.gov*** under “Reporting Forms”.

Questions regarding these reports should be addressed to Monica Posen at (212) 720-8239. Questions regarding the capital adequacy guidelines should be directed to Dianne Dobbeck in the Policy and Analysis Department at (212) 720-2610.

Sincerely,

**Signed by Kenneth P. Lamar

Kenneth P. Lamar
Assistant Vice President
Financial Reports Department

September 30, 2002

ATTACHMENT 1

Loan Commitments That Must Be Accounted for as Derivatives

FASB Statement No. 133 Implementation Issue No. C13 describes the circumstances in which a loan commitment must be accounted for as derivative. According to Issue No. C13, loan commitments that relate to the origination or purchase of mortgage loans that will be held for sale must be accounted for as derivative instruments in accordance with Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities*. However, loan commitments that relate to the origination or purchase of mortgage loans that will be held for investment, i.e., loans for which the bank holding company or its subsidiaries has the intent and ability to hold for the foreseeable future or until maturity or payoff, are not considered derivatives. In addition, commitments that relate to the origination of other types of loans (that is, other than mortgage loans) are not considered derivatives.

Mortgage loan commitments that must be accounted for as derivatives are considered over-the-counter written interest rate options. Therefore, because they are derivatives, these commitments should not be reported as unused commitments in item 1 of Schedule HC-L, Derivative and Off-Balance Sheet Items. Instead, mortgage loan commitments that are derivatives must be reported on the balance sheet (Schedule HC) at fair value. In addition, the par value of the mortgage loans to be acquired under these commitments must be reported in Schedule HC-L, item 11.d.(1), column A, and in Schedule HC-L, item 13, column A. The fair value of these mortgage loan commitments must be reported in the appropriate subitem of Schedule HC-L, item 14.b. As written options, mortgage loan commitments that are derivatives are not covered by the agencies' risk-based capital standards.

The unused portion of loan commitments that are not considered derivatives should continue to be reported in Schedule HC-L, item 1. Unused commitments with an original maturity exceeding one year are subject to the risk-based capital standards and must be reported in Schedule HC-R, item 53.

Equity-Indexed Certificates of Deposit

Under FASB Statement No. 133, a certificate of deposit (CD) that pays "interest" based on changes in an equity securities index is a hybrid instrument with an embedded derivative that must be accounted for separately from the host contract, i.e., the CD. One such equity-indexed CD is a trademarked product called the "Index Powered CD," which is sponsored by the Federal Home Loan Banks for issuance by their member depository institutions.

At the maturity date of a typical equity-indexed CD, the holder of the CD receives the original amount invested in the CD plus some or all of the appreciation, if any, in an index of stock prices over the term of the CD. Thus, the equity-indexed CD contains an embedded equity call option. To manage the market risk of its equity-indexed CDs, a bank that issues these CDs normally enters into one or more separate freestanding equity derivative contracts with an overall term that matches the term of the CDs. At maturity, these separate derivatives are expected to provide the bank with a cash payment in an amount equal to the amount of appreciation, if any, in the same stock price index that is embedded in the CDs, thereby providing the bank with the funds to pay the "interest" on the equity-indexed CDs. During the term of the separate freestanding equity derivative contracts, the bank will periodically make either fixed or variable payments to the counterparty on these contracts.

When a subsidiary bank of a bank holding company issues an equity-indexed CD, it must account for the written equity call option embedded in the CD separately from the CD host contract. The fair value of this embedded derivative on the date the CD is issued must be deducted from the amount the purchaser invested in the CD, creating a discount on the CD that must be amortized to interest expense over the term of the CD using the effective interest method. This interest expense should be reported in the income statement, of the FR Y-9C, in the appropriate subitem of Schedule HI, item 2.a, "Interest on deposits." The equity call option must be "marked to market" at least quarterly with any changes in the fair value of the option recognized in earnings. On the balance sheet, the carrying value of the CD host contract and the fair value of the embedded equity derivative may be combined and reported together as deposit liabilities on the balance sheet (Schedule HC). As for the separate freestanding derivative contracts the bank enters into to manage its market risk, these derivatives must be carried on the balance sheet as assets or liabilities at fair value and "marked to market" at least quarterly with changes in their fair value recognized in earnings. The periodic payments to the counterparty on these freestanding derivatives must be accrued with the expense reported in earnings along with the change in the derivative's fair value. In the FR Y-9C income statement (Schedule HI), the changes in the fair value of the embedded and freestanding derivatives, including the effect of the accruals for the payments to the counterparty on the freestanding derivatives, should be netted and reported consistently in either "Other noninterest income" (item 5.l) or "Other noninterest expense" (item 7.d).

The notional amounts of the embedded and freestanding equity derivatives must be reported in column C of Schedule HC-L, items 11.d.(1) and 11.e, respectively. The notional amounts of both derivatives must also be included in Schedule HC-L, item 13, column C. The fair values of these two derivative contracts must be included in the appropriate subitems of Schedule HC-L, item 14.b, column C. The equity derivative embedded in the indexed CD is a written option, which is not covered by the agencies' risk-based capital standards. However, the freestanding equity derivative is covered by these standards.

Bank holding companies or their subsidiaries that purchases an equity-indexed CD for investment purposes must account for the embedded purchased equity call option separately from the CD host contract. The fair value of this embedded derivative on the date of purchase must be deducted from the purchase price of the CD, creating a discount on the CD that must be accreted into income over the term of the CD using the effective interest method. This accretion should be reported in the FR Y-9C income statement in Schedule HI, item 1.c. The embedded equity derivative must be "marked to market" at least quarterly with any changes in its fair value recognized in earnings. These fair value changes should be reported consistently in either "Other noninterest income" (item 5.l) or "Other noninterest expense" (item 7.d). The carrying value of the CD host contract and the fair value of the embedded equity derivative may be combined and reported together as interest-bearing balances due from other depository institutions on the balance sheet in Schedule HC, item 1.b. The notional amount of the embedded derivative must be reported in Schedule HC-L, item 11.d.(2), column C, and item 13, column C, and, if appropriate, its fair value (which will always be positive or zero, but not negative) must be reported in Schedule HC-L, item 14.b.(1), column C. The embedded equity derivative in the indexed CD is a purchased option, which is subject to the agencies' risk-based capital standards.

FASB Statements Nos. 141 and 142

In July 2001, the FASB issued Statement No. 141, *Business Combinations*, and Statement No. 142, *Goodwill and Other Intangible Assets*. Statement No. 141 supersedes the previous accounting standard on business combinations (i.e., mergers and acquisitions), Accounting Principles Board (APB) Opinion No. 16, and requires that all business combinations initiated after June 30, 2001, (except for combinations between two or more mutual enterprises) must be accounted for by the purchase method. The use of the pooling-of-interests method for those business combinations is prohibited. Statement No. 141 also changes the requirements for recognizing intangible assets as assets apart from goodwill in business combinations accounted for by the purchase method for which the date of acquisition is July 1, 2001, or later. The statement specifically identifies core deposit intangibles as one type of intangible that must be recognized as an asset separate from goodwill.

Statement No. 142 supersedes the previous accounting standard on intangible assets, APB Opinion No. 17. This new standard addresses how intangible assets that are acquired individually or with a group of other assets (but not in a business combination) should be accounted for upon their acquisition. It also explains how goodwill and other intangible assets should be accounted for after they have been acquired.

Under Statement No. 142, goodwill acquired in a business combination for which the acquisition date is after June 30, 2001, should not be amortized, but should be tested for impairment in accordance with the provisions of this accounting standard. Goodwill acquired in a business combination, for which the acquisition date is before July 1, 2001, should continue to be amortized until an institution first applies all of the provisions of Statement No. 142 in accordance with the effective date of the standard. Statement No. 142 is effective for fiscal years beginning after December 15, 2001. For bank holding companies with a calendar year fiscal year, Statement No. 142 takes effect January 1, 2002.

Bank holding companies must adopt FASB Statements No. 141 and 142 for FR Y-9C reporting purposes in accordance with the effective dates of these standards based on their fiscal years. The March 2002 instruction book update included a revised Glossary entry for "business combinations;" revised instructions for Schedule HC, item 10.a, "Goodwill," and Schedule HC-M, item 12, "Intangible assets other than goodwill," and instructions for new Schedule HI, item 7.c.(1), "Goodwill impairment losses," all of which incorporated relevant provisions of these new standards.

Banks holding companies should also note that any unidentifiable intangible assets recorded in accordance with FASB Statement No. 72 should not be reported as "Goodwill" on the balance sheet (Schedule HC). Rather, these unidentifiable intangible assets should be reported in Schedule HC, item 10.b, "Other intangible assets," and must continue to be amortized. The amortization expense should be reported in item 7.c.(2) of the income statement (Schedule HI).

Upon the adoption of Statement No. 142, bank holding companies should report any impairment losses on goodwill and other intangible assets that must be recognized as a result of the standard's required transitional impairment testing as the effect of a change in accounting principle. The effect of the accounting change and related income tax effects should be reported in the income statement, Schedule HI, item 12, "Extraordinary items, net of applicable taxes and minority interest" and disclosed in Schedule HI, Memoranda item 8.

For purposes of reporting in the FR Y-9LP report, goodwill that is recorded on the parent’s books and not “pushed down” to the subsidiary or reporting unit level for accounting and reporting purposes should be *tested* for impairment at the appropriate reporting unit level as if the goodwill resides on the books of the reporting unit. Any goodwill impairment losses that result from performing the impairment test should be *recognized* on the parent's books for reporting purposes.

Although the accounting rules for goodwill and other intangible assets have changed, there has been no change in the regulatory capital treatment of these assets. The existing regulatory capital limits on servicing assets and purchased credit card relationships remain in effect, and goodwill and other intangible assets will continue to be deducted from capital and assets in determining a bank holding company's capital ratios.

Bank holding companies are encouraged to consult with their outside accountants concerning the implementation of these two new accounting standards.

Investments in Trust Preferred Securities

Bank holding companies and their subsidiaries may invest in trust preferred securities, which are hybrid instruments possessing characteristics typically associated with debt obligations. Although each issue of these securities may involve minor differences in terms, under the basic structure of trust preferred securities a corporate issuer, such as another bank holding company, first organizes a business trust or other special purpose entity. This trust issues two classes of securities: common securities, all of which are purchased and held by the corporate issuer, and trust preferred securities, which are sold to investors. The business trust's only assets are deeply subordinated debentures of the corporate issuer, which the trust purchases with the proceeds from the sale of its common and preferred securities. The corporate issuer makes periodic interest payments on the subordinated debentures to the business trust, which uses these payments to pay periodic dividends on the trust preferred securities to the investors. The subordinated debentures have a stated maturity and may also be redeemed under other circumstances. Most trust preferred securities are subject to a mandatory redemption upon the repayment of the debentures.

Trust preferred securities meet the definition of a security in FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*. Because of the mandatory redemption provision in the typical trust preferred securities, investments in trust preferred securities would normally be considered debt securities for financial accounting purposes. Accordingly, bank holding companies should report these investments as debt securities for FR Y-9C report purposes (unless, based on the specific facts and circumstances of a particular issue of trust preferred securities, the securities would be considered equity rather than debt securities under Statement No. 115). If not held for trading purposes, trust preferred securities issued by U.S. business trusts should be reported in Schedule HC-B, item 6(a), “Other domestic debt securities.”

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ATTACHMENT 2

Significant FR Y-9C Instructions September 2002

Schedule HI, Consolidated Report of Income
"Premiums" (Memo Line 12.b) was revised to clarify that only premium revenues from insurance and reinsurance **underwriting** operations should be reported in item 12(b)(1), "Premiums on insurance related to extensions of credit" and item 12(b)(2), "All other insurance premiums." See HI-22.

Schedule HC-R, Regulatory Capital
"Preferred stock (including related surplus)" (Memo Line 3) was revised to correspond to the report form and instruct respondents to include in memo 3.b **all** cumulative preferred stock instruments included and reported in "minority interest included in consolidated subsidiaries and similar items," on Schedule HC. The criteria that the amount reported must be eligible for inclusion in Tier 1 capital was deleted.

Checklist
The checklist has been reformatted and various edits have been revised or deleted.

Significant FR Y-9LP Instructions September 2002

Schedule PC-B, Memoranda Schedule
"Notes payable to special-purpose subsidiaries that issued trust preferred securities (included in Schedule PC, item 18(b) and item 5(b) above)" (Line 16) was revised to exclude any portion of notes payable that does not directly relate to the amount of trust preferred securities issued.

Checklist
The checklist has been reformatted.

FR Y-12 Instructions September 2002
"Impact on income from items 1, 2, and 3 above" (Memo Line 3) was revised to clarify that the amount reported in this item should reflect the **pre-tax year-to-date net gain (loss)** that the nonfinancial equity investments reported on lines 1,2, and 3 had on the filer's net income (loss) (Schedule HI, Line 8 of the FR Y-9C). In addition, when calculating the net gain (loss) produced by nonfinancial equity investments that are reported on the FR Y-12, overhead or other expense related items should be

excluded.

FR Y-11Q
No revisions for this quarter.